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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 788

WILLIAM C. CHICK, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

**ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS FOR
THE FIRST CIRCUIT**

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 29-48) is reported at 7 T.C. 1414. The opinion of the Circuit Court of Appeals (R. 122-129) is reported at 166 F. 2d 337.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 27, 1948. (R. 129.) The petition for a writ of certiorari was filed on May 7, 1948. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the period of administration or settlement of the Chick estate had ended within the meaning of Section 161(a)(3) of the Internal Revenue Code and Section 19.162-1 of Treasury Regulations 103, with the result that the income for the taxable year 1940 was received as income of the residuary trust and was taxable as currently distributable income to the taxpayer-beneficiaries under Section 162(b) of the Internal Revenue Code.

STATUTES AND REGULATIONS INVOLVED

The applicable statutes and Regulations are set out in the Appendix, *infra*. pp. 11-14.

STATEMENT

The facts as found by the Tax Court (R. 31-37) and as stipulated (R. 77-103) may be summarized as follows:

The taxpayers are the children of Isaac W. Chick, who died testate on March 7, 1929, leaving an estate then valued at approximately \$2,500,000. His will, dated May 8, 1909, and several codicils thereto, were allowed for probate on March 28, 1929. (R. 31.) The will and codicils provided for a number of separate trusts for the benefit of persons designated by the decedent, and directed that the residue of the estate be transferred in trust, with directions to divide the property into

two equal shares, and to pay one-half of the income to each of the taxpayers for life, with remainders at their deaths to their issue. (R. 32, 90-93.) Under the terms of the trust the net income from each equal part of the residuary trust property is currently distributable to the taxpayers. (R. 34.)

The taxpayer William C. Chick, who was named as sole executor of the estate and as trustee of the several trusts created by the will and codicils, qualified immediately after March 28, 1929, as executor and shortly thereafter as trustee. (R. 31-32.) All of the trusts, except that comprising the residuary estate, were created, or the obligation to do so was satisfactorily discharged, within a relatively short time after decedent's death. The residuary trust was never formally set up, and the taxpayer Chick has never transferred any of the assets from himself as executor to himself as trustee; he has not filed an account as executor, nor has he identified any of the assets of the estate as assets of the residuary trust. He has not paid any income from the assets held by him either to himself or to his sister, and he has not identified or credited any part of the income received by the estate as distributable to himself and his sister as beneficiaries of the residuary trust. (R. 32, 35.)

After the death of Isaac W. Chick, tax claims in substantial amounts were asserted against his estate. A federal estate tax claim was compromised

on May 28, 1931, and a refund in respect of another tax claim was made to the estate on June 19, 1933. (R. 32-33.)

The Chick estate included 2,500 shares of stock of the Atlantic National Bank of Boston, of which the decedent had been a director. After Chick's death, the taxpayer William C. Chick, holding the shares as executor, was made a director in his father's place. The Atlantic National Bank was closed in May, 1932, because its affairs were in an unsatisfactory condition. The federal authorities asserted a stockholder's liability against the estate in connection with the shares of stock owned by it and a liability against the executor as a director of the closed bank. These claims were finally settled or disposed of during the year 1937. (R. 32, 33.)

The Chick estate also owned continuously all, except for qualifying shares, of the capital stock of John H. Pray & Sons Company, a corporation engaged in the retail selling of rugs and floor coverings in Boston. (R. 31-32.) During 1940 the taxpayer, William C. Chick, was the president and a director of this corporation. From 1932 to 1940, except for 1937, the Pray Company sustained yearly operating losses. In 1938 the company was moved to a more suitable location in Boston, where since 1941 it has had an operating profit. In order to overcome its previous losses, to pay expenses of moving to the new location, and to obtain additional working capital, the Pray Company issued and sold

in 1936 and 1939 a total of \$300,000 of preferred stock at par. All of this stock was bought by the two taxpayers individually, except for \$75,000 of such stock, which was bought at par by William C. Chick as executor, from the income of the estate. (R. 33-34.)

In 1937 it was recognized that a forced sale of the Pray Company would result in a nominal price for the inventories and almost nothing for the good will which had a substantial value. The only satisfactory course was to continue the business with a view to restoring its earning capacity and enhancing its sales value. The company has become more valuable to the estate since its removal in 1938 to its present location. (R. 34.)

In 1936 William C. Chick became ill and tried to secure a corporate trustee to take the assets and run the business so that he could resign as trustee. Ordinary trust companies refused to assume the trusteeship because the trustee would have to be responsible for the operation of the business. (R. 34.)

As ultimate facts the Tax Court found that all acts necessary to complete and wind up the administration of the Chick estate had been fully performed prior to the taxable year 1940 and that the estate was not in process of administration at any time during that year. (R. 34, 35.) It therefore held, two judges dissenting, that the income of the residuary estate for 1940 was not income received during the period of administration within the pur-

view of Section 19.162-1 of Treasury Regulations 103, which it held to be a valid interpretation of Section 161(a)(3) of the Internal Revenue Code; that even though the residuary trust had not formally been created, the trustee had in fact assumed his duties and the trust was an entity in 1940 for tax purposes; that the income for that year was received by William C. Chick, as trustee; and that, since the income was required under the terms of the will to be distributed currently to the taxpayers as life beneficiaries, it was taxable to them under Section 162(b) of the Internal Revenue Code, whether distributed to them or not. (R. 37-42, 45-48.) The Circuit Court of Appeals affirmed. (R. 122-129.)

ARGUMENT

1. Petitioners' principal ground for certiorari is an alleged conflict with *Frederich v. Commissioner*, 145 F. 2d 796 (C. C. A. 5). Although the *Frederich* case reflects an approach to the problem that is not entirely in harmony with that of both courts below in the present case, the decision is nevertheless distinguishable. Indeed the circuit court of appeals herein explicitly noted that it "express[ed] no opinion upon" the issue decided in the *Frederich* case (R. 128). In the *Frederich* case the estate under order of the local probate court, was engaged in business as a partner during, as well as subsequent to, the taxable years, and it could perhaps be deemed for federal tax purposes to be in process of administration in the taxable years, since the chief asset of the estate,

the interest in the partnership, had not then formally been reduced to possession by the estate. See Section 19.162-1 of Treasury Regulations 103 (Appendix, *infra*). In contrast, in this case all assets of the estate had been collected, all claims against the estate had been settled by the end of 1937, and the local probate court had not authorized or directed continuation of administration into the taxable year 1940. Thus, under Section 19.162-1 of Treasury Regulations 103, the period of administration had plainly ended¹ and the income for 1940 was correctly found by both lower courts to be income received by taxpayer Chick in his capacity as residuary trustee, for which position he had qualified in 1929.

Although in the *Frederich* case, the court seems to have construed the regulation as contemplating that an estate is in administration as long as it is

¹ Even if it is assumed that the executor continued administration after 1940 in order to effect an advantageous sale of the Pray Company business as a going concern (See Br. 15-16), this did not compel the Tax Court to find that the ordinary duties of administration had not been completed prior to 1940. As both lower courts emphasized (R. 41, 129), the estate owned stock of the Pray Company, rather than the business itself; the business was continued and conducted by taxpayer Chick in his capacity as president of the corporation rather than as executor of his father's estate; since the stock was completely owned by the estate it was in distributable form, and there was nothing to show why Chick could not have voted the stock in his capacity as trustee equally as well as in his capacity as executor. Taxpayers' suggestion that an executor has greater power in the disposition of estate property than does a trustee (Br. 16) does not even seem persuasive since, as taxpayers show (Br. 16), in Massachusetts a trustee may sell personal property, which would include the Pray stock here involved. Indeed, Chick himself seems to have recognized that he was really functioning as trustee rather than executor as early as 1936, since he then sought to procure a trustee to succeed himself as trustee. (R. 34.)

unsettled for purposes of local law, that interpretation apparently was devised to prevent a "disregard [of] valid orders of the probate court" (p. 798), and it can be considered in conflict with the construction given the regulation in the opinion below only if it is assumed that the Fifth Circuit Court of Appeals intended its construction of the regulation to control in the factual situation present here, where the ordinary duties of administration had long been completed and the local court had not ordered affirmatively that administration be continued beyond that time. There is no indication in the *Frederich* case that the court intended its decision to govern a situation such as is here presented.

2. There is no merit in the taxpayers' contention (Pet. 8, Br. 17-23) that the judgment below invades rights reserved to the States. The decision made pursuant to the regulation that, for federal tax purposes, the period of administration under the facts here had terminated and the income for 1940 must be attributed to the residuary trust, does not impinge upon the status of the estate or residuary trust under state law for other purposes. The regulation defines the period of administration of an estate for federal tax purposes only and, as applied to the facts here, it patently is a valid interpretation of Section 161(a)(3) of the Internal Revenue Code (Appendix, *infra*). Cf. *United States v. Britten*, 161 F. 2d 921, 927 (C.C.A. 3). The record

does not show that there has been a decree of any kind by a Massachusetts court with respect to the Chick estate or trust which the judgment below contradicts.²

Furthermore, even if it is assumed *arguendo* that under state law the estate was in the process of administration in 1940, the judgment below was correct. Since the Chick will did not direct that the income be accumulated until the residuary trust was established, the taxpayers were entitled to the income from the date of testator's death. Massachusetts General Laws, c. 197, Sec. 26 (Appendix, *infra*) ; *Sargent v. Sargent*, 103 Mass. 297 ; *Lovering v. Minot*, 63 Mass 151 ; *Pope v. Pope*, 209 Mass. 432. The net income was thus currently distributable to them by the estate and taxable to them under Section 162(b) of the Internal Revenue Code (Appendix, *infra*), whether distributed or not.

² Cases such as *Welch v. Boston*, 211 Mass. 178 (taxpayers' Br. 23), are not pertinent here. They were decided under a Massachusetts statute which requires that the executors must give notice through some authoritative act to the local tax assessors of distribution to themselves as trustees, in order to be taxed for local tax purposes as a trust, rather than as an estate, prior to the expiration of three years after the appointment of the executors. Cf. *Hines v. Levers & Sargent Co.*, 226 Mass. 214; and *Mass. Inst. of Technology v. Attorney General*, 235 Mass. 288.

CONCLUSION

Since the judgment below is correct and is not in conflict with other decisions, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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JUNE 1948.

APPENDIX**Internal Revenue Code:****SEC. 161. IMPOSITION OF TAX.**

(a) *Application of Tax.*—The taxes imposed by this chapter upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

* * * *

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

* * * *

(b) *Computation and Payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for benefit of the grantor).

(26 U.S.C. 1940 ed., Sec. 161.)

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income

collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

* * * *

(26 U.S.C. 1940 ed., Sec. 162.)

II General Laws, Massachusetts (Tercentenary ed., 1932), ch 197:

SECTION 26. If an annuity, or the use, rent, income or interest of property, real or personal, is given by will or by an instrument in the nature thereof to or in trust for the benefit of a person for life or until the happening of a contingency, such person shall be entitled to receive and enjoy the same from and after the decease of the testator, unless it is otherwise provided in such will or instrument.

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.162-1. Income of estates and trusts.

* * *

From the gross income of the estate or trust there are also deductible (either in lieu of, or in addition to, the deductions referred to in

the preceding paragraph of this section) the following:

* * * *

(2) Any income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to a beneficiary, whether or not such income is actually distributed.

* * * *

Any amount described in paragraph (2) or (3) of this section as being deductible from the gross income of the estate or trust shall be included in computing the net income of the legatees, heirs, or beneficiaries, whether distributed to them or not.

* * * *

The income of an estate of a deceased person, as dealt with in the Internal Revenue Code, is therein described as received by the estate during the period of administration or settlement thereof. The period of administration or settlement of the estate is the period required by the executor or administrator to perform the ordinary duties pertaining to administration, in particular the collection of assets and the payment of debts and legacies. It is the time actually required for this purpose, whether longer or shorter than the period specified in the local statute for the settlement of estates. If an executor, who is also named as trustee, fails to obtain his discharge as execu-

tor, the period of administration continues up to the time when the duties of administration are complete and he actually assumes his duties as trustee, whether pursuant to an order of the court or not. * * *